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# In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 212

KAUFMANN AND BAER COMPANY

AND

GIMBEL BROTHERS, INC., PETITIONERS

*v.*

UNITED STATES OF AMERICA

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS*

## BRIEF FOR THE UNITED STATES IN OPPOSITION

### OPINION BELOW

The opinion of the Court of Claims (Pet. 27–36) is reported at 137 F. Supp. 725.

### JURISDICTION

The judgment of the Court of Claims was entered on January 31, 1956. The petition for a writ of certiorari was filed on June 28, 1956, the time for filing having been extended to June 29, 1956. The jurisdiction of this Court is invoked under 28 U. S. C. 1255 (1).

### QUESTION PRESENTED

Whether the taxpayer made a valid election to adopt for the fiscal year ending January 31, 1942, the last-in, first-out method of valuing inventories (commonly known as LIFO) under Section 22 (d) (2) of the Internal Revenue Code of 1939, as amended, so as to entitle it to have its taxable income for that year computed on that basis.

### STATUTE AND OTHER AUTHORITIES INVOLVED

The statute and other authorities involved are sections 22 and 3772 of the Internal Revenue Code of 1939, Sections 19.22 (d)–1, 19.22 (d)–2, 19.22 (d)–3 and 19.22 (d)–5 of Treasury Regulations 103, and Mim. 6244, 1948–1 Cum. Bull. 21. All are set forth in the Appendix, *infra*, pp. 20–27.

### STATEMENT

The pertinent facts, in the main set forth in the findings of fact of the Court of Claims (Pet. 36–55), are as follows:

Gimbel Brothers, Inc., herein referred to as Gimbels, is a New York corporation engaged in the business of operating department stores. It maintains its principal office and place of business in the City of New York. (Pet. 37.)

From March 15, 1926, until January 31, 1946, Kaufmann and Baer Company, a Pennsylvania corporation owning and operating a retail department store in Pittsburgh, Pennsylvania, was a wholly owned subsidiary of Gimbels. On the latter date, Kaufmann and Baer, herein referred to as taxpayer, was dissolved and all of its assets were transferred to its parent, Gimbels. (Pet. 36–38.)

Kaufmann and Baer kept its books and filed its federal tax returns on an accrual method of accounting

for fiscal years ending January 31. Because it is not practicable to control inventories of department stores on an item basis, the industry early developed the retail method of taking inventory, which has long been approved by Treasury regulations and was at all times used by Kaufmann and Baer in computing the cost of goods sold. (Pet. 38, 47.)

Under the retail method of inventorying, the total merchandise carried is broken down into classifications (such as women's coats, men's suits, appliances, etc.), each of which is given a department name and number. In computing the closing inventory, a dollar figure is arrived at for each department by cumulating the retail prices for all merchandise in the department as of the closing inventory date. This value is converted to cost by applying the mark-on per cent.[1] The resultant figure is the closing inventory for the department. The sum of the closing inventories for all departments represents the closing inventory for the store, which figure is credited to the cost-of-goods-sold account in arriving at gross profit. (Pet. 40–41.)

For all years up to and including the fiscal year ended January 31, 1941, Kaufmann and Baer employed the retail method of taking inventories on a first-in, first-out basis (commonly known as FIFO), as

[1] The mark-on per cent represents the average net markup for the department converted to a percentage of average retail sales. The average net markup is computed for each department by adding purchases at cost to the opening inventory at cost, and subtracting this figure from the total of opening inventory at retail plus purchases at retail. The result, when divided by the opening inventory at retail plus purchases at retail (with proper adjustments for all markups and markdowns), yields the mark-on per cent. (Pet. 40–41.)

opposed to last-in, first-out (LIFO).[2] During periods of rising prices, the use of LIFO will reflect smaller profits than will the use of FIFO.[3] (Pet. 41–43.)

Section 22 (d) of the Internal Revenue Code of 1939 made the elective method of inventorying goods (LIFO) available generally to all taxpayers who could meet the requirements therein established. These requirements were in part that the inventory must be valued at cost, and that no method other than LIFO shall have been used for any period beginning with or during the first taxable year for which LIFO was to be used. Under the section as it read prior to its amendment on October 21, 1942, LIFO could not be adopted beginning with a taxable year during any part of which another inventory method had been used for purposes of interim or annual reports to shareholders or creditors. Kaufmann and Baer had prepared an interim statement for the period February 1, 1941, to July 31, 1941, which did not reflect the use of LIFO, and which was included in a consolidated statement of Gimbels presented in an

[2] The FIFO method assumes that the first goods purchased were the first ones sold, so that the ending inventory is made up of the last merchandise purchased. Under LIFO it is assumed that the last goods purchased were the first sold. (Pet. 41–42.)

[3] During periods of price fluctuations the gross profit tends not to be stable under FIFO because, for example, during a rising price period the ending inventory will be inflated (reflecting as it does the high prices of the latest goods purchased), thus reducing cost-of-goods-sold, and increasing gross profit. During a price decline the ending inventory will be reduced, which will reduce the gross profit. Under LIFO, however, the gross profit is stabilized somewhat because the ending inventory is presumed to be composed of merchandise purchased before the price inflation or deflation, as the case may be. (Pet. 41–43.)

interim report to Gimbels' stockholders. Therefore, under Section 22 (d) as it then read, Kaufmann and Baer was ineligible to use LIFO for the fiscal year ended January 31, 1942. (Pet. 44.)

From 1942 until 1948, the Internal Revenue Bureau maintained the position that LIFO was available only if applied to the actual cost of specific items of merchandise. Section 22 (d) (2) (A) permitted LIFO only as to "goods * * * specified in an application to use such method". Therefore, the Internal Revenue Bureau reasoned that it was not available to taxpayers using the retail inventory method because such inventory represented the estimated cost of groupings of goods stated in terms of dollar values rather than an itemized list of the cost of each article. (Pet. 43, 47.) Accordingly, the regulations made no provision for the use of ~~such~~ price indices reflecting relative changes in market prices. (Pet. 43.) Such indices would be required to apply LIFO to the retail inventory method.

Section 118 of the Revenue Act of 1942, effective October 21, 1942, amended Section 22 (d) of the Internal Revenue Code so as to remove the prohibition against the use of LIFO during a year in which interim reports showed that a non-LIFO method had been used. The amendment was retroactive to taxable years beginning after December 31, 1938. (Pet 44, 45.)

Touche, Niven and Company were the accountants for Gimbels and its subsidiaries, including Kaufmann and Baer. Mr. Friedman of Touche, Niven antici-

pated that Section 22 (d) would be amended so as to remove the interim report obstacle. In accordance with his recommendation, Gimbels' directors decided to adopt LIFO for the fiscal year ended January 31, 1942, and so informed the stockholders in the annual report for that year dated April 11, 1942. (Pet. 45; R. 122–123.) The federal tax returns were due on April 15, 1942, but an extension was obtained in the hope that the amendment removing the interim report obstacle would be passed quickly. It was decided to file the returns by July 15 on the FIFO basis and, if the law was amended, to file either amended returns or claims for refund. The returns were filed on July 13, 1942, on a non-LIFO basis, and all returns thereafter until 1948 were filed on a non-LIFO basis. (Pet. 38; R. 123–124.)

Section 22 (d) of the 1939 Code, as amended by Section 118 of the Revenue Act of 1942, which eliminated the interim report obstacle, provided that the change to the LIFO method should be in accordance with regulations to be promulgated by the Commissioner. Accordingly, Section 19.22 (d)–3, Treasury Regulations 103, was amended by T. D. 5199, 1942–2 Cum. Bull. 81, approved December 10, 1942, so as to read in part as follows:

> *Time and manner of making election.*—The elective inventory method may be adopted and used only if the taxpayer files with his return for the taxable year as of the close of which the method is first to be used (or, if such return is filed prior to March 10, 1943, the ninetieth day after the approval of Treasury Decision

> 5199, then at any time prior to such date) in triplicate on Form 970 (revised), and pursuant to the instructions printed thereon and to the requirements of this section, a statement of his election to use such inventory method. * * *

T. D. 5199 was first published in the Federal Register on December 12, 1942. (Pet. 47–48.)

At a meeting of the executives of Gimbels and the taxpayer in December, 1942, at which meeting Mr. Friedman was present, it was decided to file elections on Form 970 to adopt LIFO for the fiscal year ended January 31, 1942, and, based on such election, to file claims for refund for that year. Mr. Friedman was instructed to prepare the necessary elections and claims for refund. Because the attitude of the Internal Revenue Bureau had been against permitting retailers to employ LIFO, Mr. Friedman did not think the time limit in T. D. 5199 applied to the taxpayer and did not request an extension of time to file Form 970 after March 10, 1943. (Pet. 48, 49.) Mr. Friedman knew that it was accepted practice to ask for extensions of time to file returns, if needed, and that such requests for extensions were ordinarily granted. (R. 148.) For example, the original returns for the fiscal year ended January 31, 1942, were filed late as the result of obtaining such an extension. (R. 123–124.)

Touche, Niven and Company prepared the claims for refund and the elections on Form 970 (Rev.), which differed very little from the old Form 970. These documents were delivered to the taxpayer on

March 25, 1943, executed March 29, 1943, and filed with the Collector of Internal Revenue at Pittsburgh on March 31, 1943. Form 970 (Rev.) was available at the end of February, 1943. (Pet. 38–39, 49; R. 140–141.)

Based on Mr. Friedman's advice that the Bureau of Internal Revenue was adamant in its position against permitting retailers to use LIFO, and that it was burdensome to keep books on LIFO while filing returns on FIFO, it was decided at a meeting of the board of directors of Gimbels on April 20, 1943, to return to FIFO. An annual report covering the operations of Gimbels and its subsidiaries, including taxpayer, for the year ended January 31, 1943, was issued the stockholders on April 24, 1943, stating inventories on the basis of FIFO. (Pet. 50.)

Thereafter, taxpayer notified the Collector at Pittsburgh on April 28, 1943, and the Commissioner of Internal Revenue at Washington on May 5, 1943, that it desired to withdraw its claim for refund for $106,287.97 and its application for change in inventory method filed on March 31, 1943. (Pet. 51.) However, on August 16, 1945, taxpayer was notified by the Deputy Commissioner that the claim for refund was rejected.[4] (Pet. 39–40.) This action was commenced in the Court of Claims on August 11, 1947, within two years after August 16, 1945. (Pet. 32.)

Some 30 to 40 stores which were members of the National Retail Dry Goods Association attached to

[4] This letter also made reference to a Certificate of Overassessment in the amount of $31,486.16 allowed taxpayer for the year ended January 31, 1942, but this matter is entirely unrelated to the question of inventory adjustments. (Pet. 39–40.)

their tax returns for the year ended January 31, 1942, their elections on Form 970 to use LIFO. This was prior to the amendment of October 21, 1942. In this group were Hutzler Brothers, Federated Department Stores, Allied Department Stores, and Halle Brothers. Gimbels was a member of the Association, but did not join this group in contesting the position of the Internal Revenue Bureau. (R. 78–80.) Touche, Niven handled the accounts of Federated Department Stores and Allied Department Stores. (R. 119.) Members of the group cooperated with Hutzler Brothers, to whom a deficiency notice had been issued by the Bureau based on the disallowance of the LIFO method, in presenting a test case before the Tax Court. On January 14, 1947, the Tax Court decided in favor of adoption and use of LIFO by retail department stores. *Hutzler Brothers* v. *Commissioner,* 8 T. C. 14. The Treasury proposed drawing regulations to give relief to those retailers who had filed their elections before October 21, 1942, and who had persisted in contesting the matter, even though no new elections had ever been filed by them on Form 970 (Rev.) after October 21, 1942 (Pet. 43–44, 52–53.)

Taxpayer and Gimbels were not included in this group. Negotiations looking toward ultimate allowance of LIFO for the taxpayer were conducted, but were unsuccessful. The Internal Revenue Bureau would not allow the claim because the Form 970 election had not been filed within the time required by T. D. 5199, and because the election had been withdrawn. (Pet. 53–54.) The Court of Claims dismissed the petition on the ground that the taxpayer did not

file a timely election to change to LIFO. (Pet. 33, 36.)

**ARGUMENT**

The special facts of this case present a narrow issue which does not merit review by this Court. The decision of the Court of Claims is clearly correct. Contrary to the assertion of the taxpayer (Pet. 10),[5] the case does not involve any questions of general importance which should be settled by this Court. Moreover, there is no conflict with any Court of Appeals decision.

1. The taxpayer, in effect, concedes that its attempted election to adopt the last-in, first-out method of taking inventory (LIFO) for the fiscal year ended January 31, 1942, was untimely by the terms of T. D. 5199, 1942–2 Cum. Bull. 81,[6] which amended Treasury Regulations 103, Section 19.22 (d)–3.[7] But it contends (Pet. 10–12) that T. D. 5199 was meant to apply only to those taxpayers who were entitled under the regulations to use LIFO; that inasmuch as the Treasury Department would not recognize that LIFO was available to department store retailers under the regulations, T. D. 5199 did not apply to it; and that it was not, therefore, bound by the 90-day limitation.

This reasoning ignores, however, the central fact that the taxpayer was legally entitled to use LIFO under the regulations. While it may be that the In-

[5] Any reference to taxpayer's contention includes petitioner Gimbels, taxpayer's parent and transferee.

[6] See *supra*, pp. 6–7.

[7] The regulations as amended by T. D. 5199 are set forth in the Appendix, *infra*, pp. 23–26.

ternal Revenue Bureau construed the regulations for a time as denying LIFO to retailers, the Bureau's interpretation was rejected in *Hutzler Brothers Co.* v. *Commissioner,* 8 T. C. 14. It was there successfully urged that the existing regulations, augmenting Section 22 (d) of the 1939 Code,[8] did not exclude department store retailers from adopting LIFO. Upholding this contention, the Tax Court did not invalidate the regulations.

The taxpayer can derive no support for its position from the action of the Commissioner, after acquiescing in the *Hutzler Brothers* decision, in issuing Mim. 6244, 1948–1 Cum. Bull. 21[9] to notify district collectors and other field agents that the regulations were being amended to expressly permit retailers to use LIFO. Under the Tax Court decision, this right was available to retailers in 1942 under the then existing regulations. Mim. 6244, and T. D. 5605, 1948–1 Cum. Bull. 16, therein referred to, were issued only to clarify the effect of the *Hutzler Brothers* ruling. Nor is it significant that the old regulations provided no price indices by which retailers could convert year-end prices back to the prices prevailing at the beginning of the year. That does not indicate that retailers were thereby excluded from using LIFO. Mim. 6244 points out that, even as amended, the regulations allow retailers to prepare their own indices.

Since LIFO was available to retailers under the regulations in force in 1942 (*Hutzler Brothers* v. *Commissioner, supra*), the 90-day time limitation con-

[8] See Appendix, *infra*, pp. 23–26.

[9] See Appendix, *infra*, pp. 26–27.

tained in these regulations was, as the court below pointed out (Pet. 33–34), fully applicable to the taxpayer. Accordingly, the Court of Claims correctly held that the taxpayer's election to adopt the LIFO method was ineffective because it was not timely filed. (Pet. 36.)

2. The taxpayer contends (Pet. 16–17) that, even if the 90-day period was applicable, it was an unreasonable time within which to require it to file an election. It bases this claim on the fact that Form 970 (Rev.) was not available until the end of February, leaving little more than 10 days to file a complex form.[10]

According to the taxpayer's own theory of the case, however, it paid little heed to the time limitation because of its opinion that the limitation had no application to retailers. There is no basis for assuming that the late filing can be attributed to the lack of adequate time. (Pet. 48, 49.) In this respect, the Court of Claims found that (Pet. 35):

> Had plaintiff been aware of its rights and acted with diligence it could easily have filed its election within the 90-day period.

The Government is not to blame if the taxpayer misconstrued and thereby sat too long on its rights.

Furthermore, the taxpayer was well aware that it was accepted practice to request—and obtain, without difficulty—extensions of time to file returns. (R. 148;

[10] It should be noted that Form 970 (Rev.) differed little, if at all, from the old Form 970 already in use and available. (R. 140–141.) It was the old Form 970 on which Hutzler Brothers filed their election.

Pet. 38.) If it really felt that the 90 days was insufficient, it should have requested such an extension.

No reason appears, therefore, why vague standards of reasonableness should be substituted for the specific time limit established by the Commissioner. As the court below pointed out (Pet. 34), the time limit was clearly authorized by the statute (Section 22 (d) (3) of the 1939 Code), and "when the statute and valid regulations give a taxpayer a right it must protect and prosecute that right within the required period, or such extension thereof as may be secured, or the right is lost. Time limitations within which to make elections would be meaningless if the law were otherwise."

3. It is asserted (Pet. 13–14) that the Commissioner, by not waiving the statute of limitations for the taxpayer while allegedly waiving technical defects in the elections of other retailers, has so arbitrarily discriminated in the administration of the tax laws that his action is "inimical to the concept of equal protection of the laws" (Pet. 14).[11] Apparently this is a constitutional attack.[12]

As has been frequently noted, the Fifth Amendment contains no "equal protection" clause. See

[11] The taxpayer claims (Pet. 13) that the elections filed by the retailers who cooperated in the Hutzler Brothers litigation were invalid because those retailers had issued interim reports on a non-LIFO basis whereas, at the time of their filing, the statute provided that LIFO could not be adopted in a year during which an interim report on a non-LIFO basis had been issued.

[12] There is no claim that the Commissioner acted in derogation of his delegated powers or has exceeded his statutory authority.

*Bolling* v. *Sharpe*, 347 U. S. 497, 499. Hence, any charge of unconstitutionality based upon allegedly discriminatory federal tax treatment must be grounded on the Fifth Amendment "due process" clause. *Steward Machine Co.* v. *Davis*, 301 U. S. 548, 584; *Sunshine Coal Co.* v. *Adkins*, 310 U. S. 381, 401. It has been stated that the Federal Government is "subject to restraints less narrow and confining" than are the States under the Fourteenth Amendment "equal protection" clause. *Steward Machine Co.* v. *Davis*, *supra*, p. 584; *Bromley* v. *McCaughn*, 280 U. S. 124, 139. Admittedly, however, discrimination in the application of the tax laws might be so arbitrary and unjustifiable as to violate due process. See *Brushaber* v. *Union Pac. R. R.*, 240 U. S. 1, 24–25; *Foley Securities Corp.* v. *Commissioner*, 106 F. 2d 731, 736 (C. A. 8th). But it is clear that there has been no invidious discrimination here.

The group of retailers aligned with Hutzler Brothers, apparently anticipating that the interim report obstacle would be removed by legislation, filed elections on Form 970 when they filed their returns. Their right to elect for the year ended January 31, 1942, was authorized retroactively by legislation on October 21, 1942. The Commissioner issued T. D. 5199 requiring elections to be made by March 10, 1943, on Form 970 (Rev.), which was almost identical to the old Form 970. To have required the Hutzler group to file new elections would have exalted form over substance without any corresponding benefit. See *United States* v. *Kales*, 314 U. S. 186; *United States*

v. *Memphis Cotton Oil Co.*, 288 U. S. 62; *Cumberland Portland Cement Co.* v. *United States*, 104 F. Supp. 1010 (C. Cls.). The October amendment in effect served to reach back and validate the elections, which in all respects were already valid except for the obstacle removed by the amendment. The Commissioner did not waive any technical defects. He was on timely notice by those entitled to adopt LIFO of their elections to do so.

The taxpayer, having filed its election late, is obviously not in a position to complain of discriminatory treatment. Its situation is completely unrelated to that of the Hutzler group. In short, there was no unreasonable classification of the type condemned by the Fifth Amendment.

4. The taxpayer claims (Pet. 15–16) that the Commissioner should be equitably estopped from interposing the 90-day period of limitations.

There are several elements usually regarded as essential to equitable estoppel. There must be a misrepresentation or concealment of material facts, known to the party estopped, but unknown to the other party, who must act to his detriment in reliance upon the misrepresentation. See Pomeroy, *Equity Jurisprudence*, Section 805 (4th ed.). But the misrepresentation must originate as a statement of fact rather than one of law or opinion. *Van Antwerp* v. *United States*, 92 F. 2d 871, 875 (C. A. 9th); *United States* v. *S. F. Scott & Sons*, 69 F. 2d 728, 732 (C. A. 1st). See *Robinson* v. *Commissioner*, 100 F. 2d 847, 849 (C. A. 6th), certiorari denied, 308 U. S. 567.

The alleged misrepresentation on which the taxpayer relies was an opinion of law. Therefore, estoppel is not applicable here, for "neither the taxpayer nor the Commissioner is estopped by the previous taking of an erroneous legal position." *Commissioner* v. *American Light & T. Co.*, 125 F. 2d 365, 366 (C. A. 7th). The taxpayer cannot shift the responsibility to the Commissioner merely because he advocated an erroneous view of the law. It was well aware that the Commissioner's interpretation was being contested by the Hutzler group. Its tax advisers, Touche, Niven and Company, were the accountants for at least two of the large retailers in that group. (R. 119.)

The taxpayer suggests (Pet. 15–16) that the Commissioner could have held it to its election if prices had gone down instead of up. This is not so, and the cases cited in support are not in point. The election, having been filed late, was invalid for all purposes and revocable.[13] Nor did the Commissioner even attempt to maintain a position of being able to jump either way, as taxpayer suggests. Its claim, based upon adoption of LIFO, was rejected in 1945.

It is the taxpayer, not the Commissioner (Pet. 16), which has attempted to indulge itself in the benefits which by hindsight now appear attractive. By 1948

[13] The contention was made by the Government, but not passed upon by the Court of Claims, that there was no jurisdiction in that court, or any court, to consider the suit for refund. The claim for refund, filed on March 31, 1953, was withdrawn by the taxpayer, along with the revocable invalid election, before six months had elapsed and without the Commissioner having acted on it. See Section 3772 of the Internal Revenue Code of 1939 (Appendix, infra, pp. 22–23).

it became perfectly apparent that it would have been of great benefit tax-wise to have been on LIFO for the preceding six years. But taxpayer and Gimbels had filed on FIFO all those years. If, however, they could convince the courts that an untimely election to use LIFO for the year ended January 31, 1942, later withdrawn, was valid, there might be a chance to recoup the loss. A better illustration of hindsight would be difficult to find.

5. There is no conflict with any Court of Appeals decision.

Contrary to the taxpayer's contention (Pet. 17–18), *Pictorial Review Co.* v. *Helvering,* 68 F. 2d 766 (C. A. D. C.), is in accord with the decision below. The statute involved in *Pictorial Review* allowed corporations which were affiliated within the meaning of the section to file either separate or consolidated returns; an election once made was irrevocable. The interpretative regulations, which the court held were valid while in effect, forbade the taxpayer from including the Excella Corporation in a consolidated return for 1924 as an affiliate. The regulations were later voluntarily revised by the Commissioner so that Excella qualified as an affiliate. It was held that, since the taxpayer had enjoyed no real right of election as to Excella before the revision of the regulations, it could now elect to file an amended consolidated return for 1924 with Excella included. Here, on the other hand, the regulations after October 21, 1942, never denied the taxpayer the free choice to elect LIFO. *Hutzler Brothers* v. *Commissioner,* 8 T. C. 14. It just did not avail itself of the

opportunity to elect within the valid time limitation established. Compare *Radiant Glass Co.* v. *Burnet,* 54 F. 2d 718 (C. A. D. C.).

There is likewise no conflict with *Stockstrom* v. *Commissioner,* 190 F. 2d 283 (C. A. D. C.), also cited by the taxpayer. ( Pet. 18.) In that case, the Commissioner in 1948 had attempted to assess a gift tax deficiency for 1938 against a taxpayer who had omitted filing a return for 1938. To avoid the normal three-year statute of limitations, the Commissioner relied upon an exception in the statute to the effect that the limitations period was inapplicable where no return is filed by the taxpayer. The taxpayer's failure to file a return for 1938, however, was due to a revenue official's statement years before that no return need be filed. The court held that the Commissioner could not avail itself of the statutory exception where the taxpayer's failure to file a return is attributable to the action of the Commissioner or his representative. The difference between *Stockstrom* and the instant case is apparent. In *Stockstrom,* it was the Commissioner who sought to avoid the effect of a time limitation by relying on an omission he himself had caused. Here, it is the taxpayer who seeks to avoid the effect of a time limitation by relying on a general ruling of the Commissioner. Clearly the *Stockstrom* case does not lay down any broad principle that the Commissioner is bound by any erroneous position he should take on a legal issue. See *Goldfield Consol. Mines* v. *Scott,* 247 U. S. 126; *Automobile Club of Mich.* v. *Commissioner,* 230 F. 2d 585, 589 (C. A. 6th). Moreover, an alternative ground was relied upon in

the *Stockstrom* case. The Commissioner had obtained the facts and figures concerning the 1938 gifts from the taxpayer's books in 1941. Under Section 3612 of the 1939 Code, it was the Collector's duty to make a return from his own knowledge for the taxpayer. The court held that this duty should have been performed promptly, and could not be delayed so as to toll the statute of limitations.

**CONCLUSION**

The decision below is correct. There is no conflict in decisions, and no other reason appears which would call for review. Accordingly, it is respectfully submitted that the petition for a writ of certiorari should be denied.

OSCAR H. DAVIS,
*Acting Solicitor General.*
CHARLES K. RICE,
*Assistant Attorney General.*
ROBERT N. ANDERSON,
WALTER R. GELLES,
*Attorneys.*

JULY, 1956.

# APPENDIX

Internal Revenue Code of 1939:

SEC. 22. GROSS INCOME.

* * * * *

(c) *Inventories.*—Whenever in the opinion of the Commissioner the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer upon such basis as the Commissioner, with the approval of the Secretary, may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income.

(d) (1) [As amended by Sec. 219 (a) of the Revenue Act of 1939, c. 247, 53 Stat. 862] A taxpayer may use the following method (whether or not such method has been prescribed under subsection (c)) in inventorying goods specified in the application required under paragraph (2):

(A) Inventory them at cost;

(B) Treat those remaining on hand at the close of the taxable year as being: First, those included in the opening inventory of the taxable year (in the order of acquisition) to the extent thereof, and second, those acquired in the taxable year; and

(C) Treat those included in the opening inventory of the taxable year in which such method is first used as having been acquired at the same time and determine their cost by the average cost method.

(2) The method described in paragraph (1) may be used—

(A) Only in inventorying goods (required under subsection (c) to be inventoried) specified in an application to use

such method filed at such time and in such manner as the Commisisoner may prescribe; and

(B) [As amended by Sec. 118 (a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] Only if the taxpayer establishes to the satisfaction of the Commissioner that the taxpayer has used no procedure other than that specified in subparagraphs (B) and (C) of paragraph (1) in inventorying such goods to ascertain the income, profit, or loss of the first taxable year for which the method described in paragraph (1) is to be used, for the purpose of a report or statement covering such taxable year (i) to shareholders, partners, or other proprietors, or to beneficiaries, or (ii) for credit purposes.

(3) The change to, and the use of, such method shall be in accordance with such regulations as the Commissioner, with the approval of the Secretary, may prescribe as necessary in order that the use of such method may clearly reflect income.

(4) In determining income for the taxable year preceding the taxable year for which such method is first used, the closing inventory of such preceding year of the goods specified in such application shall be at cost.

(5) If taxpayer, having complied with paragraph (2), uses the method described in paragraph (1) for any taxable year, then such method shall be used in all subsequent taxable years unless—

(A) With the approval of the Commissioner a change to a different method is authorized; or

(B) [As amended by Sec. 118 (b) of the Revenue Act of 1942, *supra*] The Commissioner determines that the taxpayer has used for any such subsequent taxable year some procedure other than that spec-

ified in subparagraph (B) of paragraph (1) in inventorying the goods specified in the application to ascertain the income, profit, or loss of such subsequent taxable year for the purpose of a report or statement covering such taxable year (i) to shareholders, partners, or other proprietors, or beneficiaries, or (ii) for credit purposes; and requires a change to a method different from that prescribed in paragraph (1) beginning with such subsequent taxable year or any taxable year thereafter.

In either of the above cases, the change to, and the use of, the different method shall be in accordance with such regulations as the Commissioner, with the approval of the Secretary, may prescribe as necessary in order that the use of such method may clearly reflect income.

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(26 U. S. C. 1952 ed., Sec. 22.)

SEC. 3772. SUITS FOR REFUND.

(a) *Limitations.*—

(1) *Claim.*—No suit or proceeding shall be maintained in any court for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected until a claim for refund or credit has been duly filed with the Commissioner, according to the provisions of law in that regard, and the regulations of the Secretary established in pursuance thereof.

(2) *Time.*—No such suit or proceeding shall be begun before the expiration of six months from the date of filing such claim unless the Commissioner renders a decision thereon within that time, nor after the expiration of two years from the date of mailing by registered mail by the Commissioner to the taxpayer of a notice of the disallowance of the part of the claim to

which such suit or proceeding relates.
(26 U. S. C. 1952 ed., Sec. 3772.)

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Treasury Regulations 103, promulgated under the Internal Revenue Code of 1939:

SEC. 19.22 (d)–1 [as amended by T. D. 5605, 1948–1 Cum. Bull. 16]. *Inventories under elective method.*—Any taxpayer permitted or required to take inventories pursuant to the provisions of section 22 (c), and pursuant to the provisions of sections 19.22 (c)–1 to 19.22 (c)–8, inclusive, may elect with respect to those goods specified in his application and properly subject to inventory to compute his opening and closing inventories in acordance with the method provided by section 22 (d). * * *

* * * * *

If a taxpayer using the retail method of pricing inventories, authorized by section 19.22 (c)–8, elects to use in connection therewith the elective inventory method authorized by section 22 (d) of the Code, the apparent cost of the goods on hand at the end of the year, determined pursuant to section 19.22 (c)–8, shall be adjusted to the extent of price changes therein taking place subsequent to the close of the preceding taxable year. The amount of any apparent inventory increase or decrease to be eliminated in this adjustment shall be determined by reference to acceptable price indices established to the satisfaction of the Commissioner. Price indices prepared by the United States Bureau of Labor Statistics which are applicable to the goods in question will be considered acceptable to the Commissioner. Price indices which are based upon inadequate records, or which are not subject to complete and detailed audit within the Bureau, will not be approved.

SEC. 19.22 (d)–2 [As amended by T. D. 5163, 1942–2 Cum. Bull. 80. and T. D. 5605, *supra*].

*Requirements incident to adoption and use of elective method.*—Except as otherwise provided in section 19.22 (d)–1 with respect to retail inventory computations, the adoption and use of the elective inventory method is, by section 22 (d) and regulations thereunder, made subject to the following requirements:

(1) The taxpayer shall file an application to use such method specifying with particularity the goods to which it is to be applied;

(2) The inventory shall be taken at cost regardless of market values;

(3) Goods of the specified type included in the opening inventory of the taxable year for which the method is first used shall be considered as having been acquired at the same time and at a unit cost equal to the actual cost of the aggregate divided by the number of units on hand. The actual cost of the aggregate shall be determined pursuant to the inventory method employed by the taxpayer under the regulations applicable to the preceding taxable year with the exception that restoration shall be made with respect to any write-down to market values resulting from the pricing of former inventories;

(4) Goods of the specified type on hand as of the close of the taxable year in excess of what were on hand as of the beginning of the taxable year shall be included in the closing inventory, regardless of identification with specific invoices, at costs determined as follows:

(a) By reference to the actual cost of the goods most recently purchased or produced;

(b) By reference to the actual cost of the goods purchased or produced during the taxable year in the order of acquisition;

(c) By application of an average unit cost equal to the aggregate cost of all of the goods purchased or produced throughout the taxable year divided by the total

number of units so purchased or produced, the goods reflected in such inventory increase being considered for the purposes of section 22 (d) as having been acquired all at the same time; or

(d) Pursuant to any other proper method which, in the opinion of the Commissioner, clearly reflects income.

Whichever of the several methods of valuing the inventory increase is adopted by the taxpayer and approved by the Commissioner shall be consistently adhered to in all subsequent taxable years so long as the elective inventory method is used by the taxpayer; * * *

* * * * *

SEC. 19.22 (d)-3 [As amended by T. D. 5199, 1942-2 Cum. Bull. 81] *Time and manner of making election.*—The elective inventory method may be adopted and used only if the taxpayer files with his return for the taxable year as of the close of which the method is first to be used (or, if such return is filed prior to March 10, 1943, the ninetieth day after the approval of Treasury Decision 5199, then at any time prior to such date), in triplicate on Form 970 (revised) and pursuant to the instructions printed thereon and to the requirements of this section, a statement of his election to use such inventory method. Such statement shall be accompanied by an analysis of all inventories of the taxpayer as of the beginning and as of the end of the taxable year for which the elective method is proposed first to be used, and also as of the beginning of the preceding taxable year. * * *

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SEC. 19.22 (d)-5. *Revocation of election.*—An election made to adopt and use the elective inventory method is irrevocable, and the method once adopted shall be used in all subsequent taxable years, unless the use of another method

be required by the Commissioner, or authorized by him pursuant to a written application therefor filed with him as provided in section 19.41–2.

Mim. 6244, 1948–1 Cum. Bull. 21:

TREASURY DEPARTMENT

OFFICE OF COMMISSIONER OF INTERNAL REVENUE

Washington 25, D. C., March 9, 1948

Collectors of Internal Revenue, Internal Revenue Agents in Charge, Heads of Field Divisions of the Technical Staff, and Others Concerned:

* * * * *

3. Treasury Decision 5605, approved March 4, 1948 [page 16, this Bulletin], amends Regulations 103 and 111 to expressly permit the use of the elective inventory method by taxpayers using the retail inventory method. Certain principles are laid down for the application of the elective inventory by such taxpayers. First, since the elective method requires the use of cost, the retail selling prices of goods included in the opening inventory and purchased during the year must be adjusted for mark-downs as well as mark-ups during the year without regard to the taxpayer's previous practice with respect to mark-downs under the retail method. This requirement does not apply to retailers employing the retail inventory method without the use of the elective method. Second, the price indices employed in the adjustment of the apparent cost of goods in the closing inventory for price changes taking place during the year must be shown, to the satisfaction of the Commissioner, to be acceptable. Any price indices must be based upon sound statistical principles of construction and upon adequate records to be kept available for examination by the Bureau.

4. Arrangements have been made between representatives of the retail trade and the United States Bureau of Labor Statistics for that agency to compute and publish a series of group index numbers of retail prices, on a country-wide basis, suitable for use by individual department stores, which will be acceptable to the Commissioner. These index numbers will cover the period from 1941 to the present on a semiannual basis, and will appear semiannually in the future. The use of such indices of the Bureau of Labor Statistics is not mandatory; indices may be prepared by an individual taxpayer based upon his own data on prices and inventory quantities, if adequate, and if proof is submitted that sound statistical methods have been employed that assure reliable indices, not only for the particular year in question, but for subsequent years. Retailers who have filed, on the basis of the elective method, returns for past years which are still open, and who used indices that are not acceptable to the Commissioner, may file amended returns employing indices.

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